CERTIFICATE

Supreme Court of the United States

OCTOBER TERM, 1926

No. 766

C. O. WESTFALL

vs.

THE UNITED STATES OF AMERICA

ON CERTIFICATE FROM THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

FILED DECEMBER 10, 1926

(32,333)

(32,333)

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INDEX

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[fol. 1]

UNITED STATES CIRCUIT COURT OF APPEALS, SIXTH CIRCUIT

No. 4596

C. O. Westfall, Plaintiff in Error,

vs.

United States of America, Defendant in Error

No. 4597

C. O. Westfall, Plaintiff in Error,

vs.

United States of America, Defendant in Error

Error to the District Court of the United States for the Western District of Michigan, Southern Division

Certified to Supreme Court October 15, 1926

Before Donahue and Moorman, Circuit Judges, and Hickenlooper, District Judge

Statement of Facts

Per Curiam:

The above entitled cases involve the same transaction and were heard and submitted together.

In case No. 4596, the defendant was convicted upon an indictment charging him with unlawfully, wilfully and feloniously aiding, abetting, inciting, counseling and procuring Carl W. Himmler, who was then the branch manager of the Commercial Savings Bank of Grand Rapids, Michigan, a state banking association, which bank was then and there a member of the Federal Reserve System as defined in the Act of Congress of December 23, 1913, to misapply the moneys, property and funds of said bank with intent to injure and defraud said member bank in violation of the pro-

[fol. 2] visions of Section 5209 of the Revised Statutes of the United States.

In cause No. 4597 C. O. Westfall was convicted upon an indictment charging him, Carl W. Himmler and others with conspiracy to commit an offense against the United States, to-wit: the offense of wilfully misapplying the moneys, funds and credits of the Commercial Savings Bank of Grand Rapids, Michigan, a state banking association and a member bank of the Federal Reserve System as defined by the Act of Congress of December 23, 1913, in violation of Section 5209 of the Revised Statutes of the United States and the amendments thereto, on the part of Carl W. Himmler to be committed by him by virtue of his office and while acting as Branch Manager of the Division Avenue Branch of the Commercial Savings Bank of Grand Rapids, Michigan.

The conviction in each of these cases was based upon the same alleged unlawful transactions, to-wit: issuing a fraudulent certificate of deposit for the sum of Ten Thousand Dollars and subsequently paying such certificate from the funds of said bank.

This court has reached a conclusion upon all questions presented by the record in either case other than the question of the constitutionality of Section 9, Chapter 6 of the Federal Reserve Act of December 23, 1913.

No authorities have been cited by counsel precisely in point, but it is urged by counsel on behalf of plaintiff in error that a state bank which becomes a member of a Federal Reserve System does not thereby become an instru-[fol. 3] mentality of the federal government within the doctrines of McCullough v. Maryland, 4 Wheat., 316, 423. By way of analogy counsel for plaintiff in error also cites the Employers' Liability Cases, 207 U. S. 463, 502; Keller v. United States, 213 U. S. 138; Hammer v. Dagenhart, 247 U. S. 251 (First Child labor Case); Child Labor Tax Case, 259 U. S. 20; and Linder v. United States, 268 U. S. 5.

This question is vital and controlling in both of these cases and for this reason, we desire the instruction of the Supreme Court for the proper decision of the following question:

Question Certified

Is the provision of Section 9, Chapter 6, of the Federal Reserve Act of December 23, 1913 as amended June 21, 1917 and July 1, 1922 constitutional in so far as it provides that "such banks and the officers, agents and employes thereof shall also be subject to the provisions of and to the penalties prescribed by Section 5209 of the Revised Statutes?"

Maurice H. Donahue, Circuit Judge. Chas. H. Moorman, Circuit Judge. Smith Hickenlooper, District Judge, sitting by designation in United States Circuit Court of Appeals, Sixth Circuit.

[fol. 4] Clerk's certificate to foregoing omitted in printing.

Endorsed on cover: File No. 32,333. U. S. Circuit Court of Appeals, Sixth Circuit. Term No. 766. C. O. Westfall vs. The United States of America. (Certificate.) Filed December 10th, 1926. File No. 32,333.

UNITED STATES OF AMERICA.

THE SUPREME COURT

C. O. WESTFALL,
Plaintiff in Error,
vs.
UNITED STATES OF AMERICA,
Defendant in Error.

No. 766, October Term, 1926.

Question Certified by Circuit Court of Appeals for the Sixth Circuit.

BRIEF FOR PLAINTIFF IN ERROR.

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INDEX OF CASES.

UNITED STATES OF AMERICA.

THE SUPREME COURT

C. O. WESTFALL,
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vs.
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Defendant in Error.

No. 766, October Term, 1926.

Question Certified by Circuit Court of Appeals for the Sixth Circuit.

BRIEF FOR PLAINTIFF IN ERROR.

I.

STATEMENT OF THE CASE.

The only question involved in this case in this court is the constitutionality of Section 5209, Revised Statutes as amended, as applied to state banks and which are members of Federal Reserve banks. The question is stated by the Circuit Court of Appeals as follows:

"Is the provision of Section 9, Chapter 6, of the Federal Reserve Act of December 23, 1923, as amended June 21, 1917, and July 1, 1922, constitutional in so far as it provides that 'such banks and the officers, agents and employees thereof shall also be subject to the provisions of and to the penalties prescribed by Section 5209 of the Revised Statutes'?"

II.

ARGUMENT.

Section 5209 as amended by the Act of Sept. 26, 1918, reads as follows:

"Section 5209. Any officer, director, agent or employee of any Federal Reserve bank, or of any member bank as defined in the Act of December 23, 1913, known as the Federal Reserve Act, who embezzles, abstracts or wilfully misapplies any of the moneys, funds or credits of such Federal Reserve bank or member bank, or who, without authority from the directors of such Federal Reserve bank or member bank, issues or puts in circulation any of the notes of such Federal Reserve bank or member bank, or who, without such authority, issues or puts forth any certificate of deposit, draws any order or bill of exchange, makes any acceptance, assigns any note, bond, draft, bill of exchange, mortgage, judgment or decree, or who makes any false entry in any book, report or statement of such Federal Reserve bank or member bank, with intent in any case to injure or defraud such Federal Reserve bank or member bank, or any other company, body politic or corporate, or any individual person, or to deceive any officer of such Federal Reserve bank or member bank, or the Comptroller of the Currency, or any agent or examiner appointed to examine the affairs of such Federal Reserve bank or member bank, or the Federal Reserve Board; and every receiver of a

national banking association who, with like intent to defraud or injure, embezzles, abstracts, purloins, or willfully misapplies any of the moneys, funds, or assets of his trust, and every person who, with like intent, aids or abets any officer, director, agent, employee or receiver in any violation of this section shall be deemed guilty of a misdemeanor, and upon conviction thereof in any district court of the United States shall be fined not more than $5,000 or shall be imprisoned for not more than five years, or both, in the discretion of the court.

"Any Federal Reserve agent, or any agent or employee of such Federal Reserve agent, or of the Federal Reserve board, who embezzles, abstracts or willfully misapplies any moneys, funds or securities intrusted to his care, or without complying with or in violation of the provisions of the Federal Reserve act, issues or puts in circulation any Federal Reserve notes shall be guilty of a misdemeanor and upon conviction in any district court of the United States shall be fined not more than $5,000 or imprisoned for not more than five years, or both in the discretion of the court."

1. We insist that Congress has no power given to it by the constitution to provide a criminal penalty for the committing of an offense against the property rights of a banking association organized under state laws.

The constitution, it will be admitted, contains no express provision authorizing the incorporation of banks by Congress and of course contains no provision authorizing Congress to regulate or interfere with state banking institutions.

Throughout the whole consideration of this case, therefore, we believe that it should be constantly borne in mind that the creation of the Federal Reserve system was accomplished wholly under the implied powers of Congress. Not only has Congress created a Federal Reserve system but it has assumed that it had implied powers

authorizing the attaching of state banking institutions to that system. When this step had been taken it seemed very easy to go a step further and assume that it had implied power to take over the regulation and control of the state banks. It was easy to go still further and to attempt to punish persons who were legally strangers to the state bank but who committed some offense against its property rights. The remoteness of the final step which has been taken from the field of statutory authority defined in the constitution is a very important element to be considered in this case.

The most familiar case dealing with the power of Congress to incorporate banks is that of McCulloch vs. Maryland, 4 Wheaton, 316. In that case, which was decided in 1819, Chief Justice Marshall readily conceded that there was no express power to be found in the constitution for the establishing of a bank or creating a corporation. He explains the history of the constitution, however, particularly with reference to the implied powers which were expressly confirmed to Congress, and finally in support of the assumption of power by which Congress had created the national bank said:

> "Although, among the enumerated powers of government, we do not find the word 'bank' or 'incorporation,' we find the great powers to lay and collect taxes; to borrow money; to regulate commerce; to declare and conduct a war; and to raise and support armies and navies. The sword and purse, all the external relations, and no inconsiderable portion of the industry of the nation are intrusted to its government. It can never be pretended that these vast powers draw after them others of inferior importance, merely because they are inferior. Such an idea can never be advanced. But it may, with great reason, be contended, that a government, intrusted with such ample powers, on the due execution of which

the happiness and prosperity of the nation so vitally depends, must also be intrusted with ample means for their execution. The power being given, it is the interest of the nation to facilitate its execution. It can never be their interest, and cannot be presumed to have been their intention, to clog and embarrass its execution by withholding the most appropriate means. Throughout this vast republic, from the St. Croix to the Gulf of Mexico, from the Atlantic to the Pacific, revenue is to be collected and expended, armies are to be marched and supported. The exigencies of the nation may require, that the treasure raised in the North should be transported to the South, that raised in the East conveyed to the West, or that this order should be reversed. Is that construction of the constitution to be preferred which would render these operations difficult, hazardous and expensive? Can we adopt that construction (unless the words imperiously require it) which would impute to the framers of that instrument, when granting these powers for the public good, the intention of impeding their execution by withholding a choice of means? If, indeed, such be the mandate of the constitution, we have only to obey; but that instrument does not profess to enumerate the means by which the powers it confers may be executed; nor does it prohibit the creation of a corporation, if the existence of such a being be essential to the beneficial exercise of those powers. It is, then, the subject of fair inquiry, how far such means may be employed."

The great chief justice then proceeds to inquire what means of execution are available to Congress for carrying out the express powers and dwells at some length upon the necessity for discretion being left with Congress, in the course of which he uses that language which has become almost as well known as the constitution itself: "Let the end be legitimate, let it be within the scope of the constitution and all means which are appropriate, which are plainly adapted to that end, which are

not prohibited but consist with the letter and spirit of the constitution, are constitutional."

This rule of construction has been made use of by this court without criticism for more than a hundred years, and it is only necessary in any case to decide how the case stands in relation to that rule.

The case of McCulloch vs. Maryland is particularly interesting and valuable in this case for the reason that it involves banking institutions. In the first excerpt which we have quoted from the opinion, the chief justice called to his support every provision of the constitution which would lend strength to the act which Congress had adopted. We must remember that the proposition was a novel one at that time. The national bank had many bitter enemies. It was a subject of political debate. The essential nature of our Federal government and its constitution hinged upon the decision; by its standards political theories were to be tested. We may safely assume, therefore, that the opinion was written for the purpose of convincing its critics as well as disposing of the case then immediately at hand. Therefore if we do not find justification for a congressional enactment such as the one now involved, in the opinion in McCulloch vs. Maryland, we are not apt to find it elsewhere.

Another great test of the powers of Congress reached a crisis in the Legal Tender Cases, 12 Wallace, 457. In that case the Supreme Court divided into two communities of opinion which persisted for many years, and indeed until in the course of nature the personnel of the court had greatly changed; but even by those who adhered to the majority opinion in that case it was not maintained that Congress could exercise powers which in their nature appertained to the states unless those powers

be appropriate and conducive to the proper execution of the express powers found in the constitution.

2. The practice of gathering together within a single statute and even within a single clause powers which may be legitimately exercised and others which, while they may have some apparent relationship, are nevertheless exclusively intrastate, has been clearly condemned by this court in several cases.

The practice consists of proceeding step by step, first in the exercise of proper powers, then in the exercise of others more doubtful but which seem to sustain and extend the first, then likewise to still more doubtful assumptions to sustain the latter until the mandates of the constitution are wholly lost sight of.

A very clear example of this class of legislation is exposed in Employers Liability Cases, 207 U. S. 463. In that case this court declared invalid the first Employers Liability Act, in which in a single paragraph Congress attempted to provide regulations applicable to "every common carrier engaged in a trade or commerce in the District of Columbia or in any territory of the United States, or between the several states, etc.," whether the acts attempted to be regulated were performed in the carrying on of interstate commerce or not.

This court held that it was the duty of Congress and not the court to differentiate between its valid powers and powers which were not bestowed upon it, and that by attempting to throw both classes of legislation into one indivisible statute the act was rendered nugatory.

The danger in legislation of that sort is that it is fundamentally misleading to those whose duty it is to construe it. The Employers Liability Act at first ex-

amination contained much that was valuable and much that was clearly within the powers of Congress but, unfortunately, much was mingled with it that might be deemed generally beneficial, but nevertheless was an intrusion upon the rights of the states. In considering legislation of that character the temptation is ever present to surrender what may seem to be an unimportant state privilege in order to retain the general good which is accomplished by the valid portions of the act.

The case of Keller vs. United States, 213 U. S. 138, is a case of the type which we have mentioned. This case involved the validity of a statute which provided, among other things that any one who gave support or harbor to a female person who had immigrated to the United States within a period of three years and who engaged in immorality or was employed in a house of ill fame should be punished as provided by the statute. This court found that Congress by attempting to enact this regulation had stepped beyond the powers which were granted to it by the constitution. The decision, in effect, was that the attempted regulation was too remote from the general purpose of preventing the importation of women for immoral purposes, and the statute was declared unconstitutional.

3. The Federal government cannot, under pretext of exercising its proper constitutional powers, indirectly and circuitously dictate the internal affairs of the states. This was clearly decided in the case of Hammer vs. Dagenhart. This case held invalid the first child labor statute which provided that goods should not be transported in interstate commerce if made at a factory at which, within thirty days prior to their removal there-

from, children of certain ages had been employed under certain conditions. It was revealed by the opinion of the court that the goods produced were of themselves harmless. This fact was shown by the provision which permitted them to be shipped after thirty days from the time of their removal from the factory. It was also found that the use of interstate transportation was not a part of the evil intended to be restrained and was not necessary to its accomplishment. The court summarized its opinion as follows:

> "We have neither authority nor disposition to question the motives of Congress in enacting this legislation. The purposes intended must be attained consistently with constitutional limitations and not by an invasion of the powers of the states. This court has no more important function than that which devolves upon it the obligation to preserve inviolate the constitutional limitations upon the exercise of authority, federal and state, to the end that each may continue to discharge, harmoniously with the other, the duties entrusted to it by the constitution.
>
> "In our view the necessary effect of this act is, by means of a prohibition against the movement in interstate commerce of ordinary commercial commodities, to regulate the hours of labor of children in factories and mines within the states, a purely state authority. Thus the act in a two-fold sense is repugnant to the constitution. It not only transcends the authority delegated to Congress over commerce but also exerts a power as to a purely local matter to which the federal authority does not extend. The far-reaching result of upholding the act cannot be more plainly indicated than by pointing out that if Congress can thus regulate matters entrusted to local authority by prohibition of the movement of commodities in interstate commerce, all freedom of commerce will be at an end, and the power of the states over local matters may be eliminated, and thus our system of government be practically destroyed."

Congress was not to be deterred so easily, however, and as a result adopted the Act of February 24, 1919, 40 Stat. 1057-1138. In this statute a very heavy tax was levied upon the net profits of any institution for the taxable year during any part of which children have been employed or permitted to work under certain conditions. The court, however, held that Congress had again exceeded its authority and had attempted, under the guise of taxation to regulate the intimate details of affairs which were constitutionally reserved to the control of the states. The following remarks of the chief justice are particularly important:

> "The good sought in unconstitutional legislation is an insidious feature because it leads citizens and legislators of good purpose to promote it without thought of the serious breach it will make in the ark of our covenant, or the harm which will come from breaking down recognized standards. In the maintenance of local self-government on the one hand and the national power on the other our country has been able to endure and prosper for nearly a century and a half."

The chief justice also quotes the following from McCulloch vs. Maryland:

> "Should Congress in the execution of its powers adopt measures which are prohibited by the constitution, or should Congress under the pretext of its powers pass laws for the accomplishment of objects not intrusted to the government, it would become the painful duty of this tribunal, should a case requiring such a decision come before it, to say that such an act was not the law of the land."

The case of Linder vs. United States, 268 U. S. 5; 45 Sup. Ct. 446, is a very clear illustration of the rule which

limits Congress to the accomplishment of those objects intrusted to it by the constitution, even though it might be deemed convenient and wholesome for the public good for Congress also to administer police powers reserved to the states. The specific instance covered by that case was an alleged offense under the Harrison Anti-Narcotic law. Mr. Justice McReynolds says:

> "Obviously direct control of medical practice in the states is beyond the power of the Federal government. Incidental regulation of such practice by Congress through a taxing act cannot extend to matters plainly inappropriate and unnecessary to a reasonable enforcement of a revenue measure."

And again he says:

> "The narcotic law is essentially a revenue measure, and its provisions must be reasonably applied with the primary view of enforcing the tax. We find no facts alleged in the indictment sufficient to show that petitioner had done anything falling within definite inhibitions, or sufficient materially to imperil orderly collection of revenue from sales. Federal power is delegated, and its prescribed limits must not be transcended, even though the end seems desirable."

It is submitted that these decisions clearly establish, first, that if it is appropriate and conducive to some constitutional object, Congress may exercise powers which if applied to state matters would have been exclusively within state control; and second, Congress cannot exercise any police powers generally reserved to the states which are not appropriate and conducive to the accomplishment of some constitutional object, even though such a police power may be convenient and closely related to the general subject of legislation and of actual public benefit.

4. It has been repeatedly held by this court that if a statute inseparably embraces legislation which is constitutionally valid with legislation which is invalid, then the whole act must fall together. Congress will not be permitted to stand with one foot on legal ground and with the other trespass upon grounds which are forbidden to it.

One of the leading cases on this subject is United States vs. Reese, 92 U. S. 214. The court had under consideration in that case a statute enacted by Congress ostensibly for the purpose of carrying into execution the provisions of the fifteenth amendment and to prevent discrimination in the exercise of the elective franchise on account of race, color or previous condition of servitude. Certain sections of the statute, however, which were inseparable in effect from the rest of the statute, provided penalties for offenses which were not within the constitutional authority of Congress, at the same time covering other acts which were within its constitutional powers. The court held that the whole statute must fail, saying:

> "We are, therefore, directly called upon to decide whether a penal statute enacted by Congress, with its limited powers, which is in general language broad enough to cover wrongful acts without as well as within the constitutional jurisdiction, can be limited by judicial construction so as to make it operate only on that which Congress may rightfully prohibit and punish. For this purpose, we must take these sections of the statute as they are. We are not able to reject a part which is unconstitutional,
>
> and retain the remainder, because it is not possible to separate that which is unconstitutional, if there be any such, from that which is not. The proposed effect is not to be attained by striking out or disregarding words that are in the section, but by in-

serting those that are now there. Each of the sections must stand as a whole, or fall altogether. The language is plain. There is not room for construction, unless it be as to the effect of the constitution. The question, then, to be determined, is, whether we can introduce words of limitation into a penal statute so as to make it specific, when, as expressed, it is general only.

"It would certainly be dangerous if the legislature could set a net large enough to catch all possible offenders, and leave it to the courts to step inside and say who could be rightfully detained, and who should be set at large. This would, to some extent, substitute the judicial for the legislative department of the government. The courts enforce the legislative will when ascertained, if within the constitutional grant of power. Within its legitimate sphere, Congress is supreme, and beyond the control of the courts; but if it steps outside of its constitutional limitations, and attempts that which is beyond its reach, the courts are authorized to, and when called upon in due course of legal proceedings must, annul its encroachments upon the reserved power of the states and the people."

The foregoing case was cited and followed in the Trade-Mark Cases, 100 U. S. 82, in which the court had before it a statute in which Congress attempted to regulate the use of trade-marks in intrastate business as well as in affairs properly within the control of Congress. The court again held that it could not amend the statute so as to make it applicable only in its valid parts, as the provisions were apparently adopted with one general purpose and such a construction would amount to legislation.

The same rule is again applied in Baldwin vs. Franks, 120 U. S. 678; Spraigue vs. Thompson, 118 U. S. 90; Pollock vs. Farmers Loan & Trust Company, 158 U. S. 608.

5. The statute which is under consideration in the present case exceeds the power granted to Congress by the constitution in attempting to interfere with purely state affairs. The Commercial Savings Bank, whose property rights are alleged to have been invaded in the present case, is a purely state institution. It was organized under a statute which was enacted long before the Federal Reserve act was drafted, although we do not need to say that priority in time is in any wise controlling. We refer to it only to emphasize the point under discussion. It is clear from an examination of the Federal Reserve act that no attempt is made to change the character of state banking corporations. We need not discuss whether or not such an attempt would be constitutional if made.

State banks are invited by the statute to become members of the Federal Reserve banks of the several districts in which they are located. Becoming a member of Federal Reserve banks consists principally in buying a certain amount of capital stock in the Federal Reserve bank. The relationship thereafter existing between the Federal Reserve bank and the member bank is that of corporation and stockholder, and may also from time to time be that of debtor and creditor, the Federal Reserve bank being authorized to purchase negotiable paper from the member bank and also to lend money to the member bank upon such conditions as will insure the safety thereof.

The member bank upon its admission to membership submits itself to examinations to be made of its financial condition by the examiners acting under the Federal government. We insist that there is nothing in these practices which change the character of the bank from that of a state institution to that of an instrumentality

of the national government. The national banks have always been sustained as creatures of Congress upon the assumption that they are instrumentalities of the Federal government.

McCulloch vs. Maryland, 4 Wheat. 316.
Legal Tender Case, 110 U. S. 445.
United Statss Bank vs. Georgia State Bank, 10 Wheat. 333.

There seems to be no reason to doubt that it is as necessary and appropriate for the state to have state banks for the convenience of its citizens, the prosperity of its people and the carrying on of its governmental affairs as it is for the national government to establish national banks for its proper purposes. It has been deemed necessary for the national government to have its own banks under its own domination and control. We submit that it is equally necessary that the state have its state banks under its exclusive control, at least in the carrying on of ordinary state affairs.

The act under discussion (Revised Statutes, Sec. 5209) assumes to punish persons committing certain offenses against a state bank. The best reason which could be argued, in support of such a statute, would be that it was adopted for the purpose of protecting the Federal Reserve banks from possible losses due to the inroads which might be made by fraud upon the resources of state banks, who might at the time be debtors to the Federal Reserve banks. It cannot be argued that such offenses will in any wise menace a Federal Reserve bank on account of the relationship of the member banks as stockholders because under the provision of the Federal Reserve act stock is not issued to the state banks except as paid for.

But if it was the intention of Congress to protect the Federal Reserve banks as creditors from possible impairment of the resources of the member banks as debtors, that object could have been readily accomplished by provisions appropriate to that end. We do not need to question at this time whether the Federal government could punish crimes which constitute a menace to the Federal Reserve bank in its immediate relationship with the member bank. For instance, if a penalty were imposed upon one who abstracted funds which were in the course of transmission from the member bank to the Federal Reserve bank, it would present an entirely different question, but the act in question proposes to punish those who commit offenses against a member bank, which may be or which may not be a debtor of the Federal Reserve bank. It proposes to punish for an offense which may or may not impair the resources of a debtor of the Reserve bank. The statute attempts to legislate upon strictly state affairs in the same section and in the same clause in which it attempts to correct possible evils which may affect Federal bank affairs.

In attempting to seize upon a specific power to be used for a specific purpose Congress sweeps into its control a myriad of instances with which it has no concern.

It would be a very radical assertion to claim that the Federal government may assume control and regulation over all persons and institutions who may be debtors to national banks. This would extend the national power to matters which are intrinsically local in their nature. If it were carried to its logical culmination, state authority would become but a shadow. Every industry and every commercial institution which borrowed money from a national bank would then receive its instructions from Washington and would look to Congress for its

existence, regulation and protection. It is hard to imagine anything that would be left for the states to regulate. If the creditor and debtor relationship can be made the foundation for extending the powers of the national government then we have taken the most important and revolutionary step that has yet been attempted. This is not a conjectural possibility but is the very foundation of the government's contention in the present case.

The language of the statute is so broad that it applies to offenses committed against state banks even in those instances in which the offense can not possibly result in any loss or inconvenience to the Federal Reserve bank. This being an inseparable feature of the act, we submit that the act must fail unless all of the offenses covered by it can be shown to be within the authority of Congress to punish.

6. It may be contended in support of the statute that the Federal Reserve act was designed to create a national system of banks which would include all state banks which might elect to attach themselves to it. This contention can not be sustained, because Congress can not by providing broad and comprehensive regulations for the control of a subject within its constitutional authority invade the fields of legislation which are reserved to the states.

This is well illustrated by the distinction which has been persistently made by this court between interstate commerce and intrastate commerce. The first great decision under the commerce clause was Gibbons vs. Ogden, 9 Wheat. 1. In that case Chief Justice Marshall wholly sustained the power of Congress to regulate interstate commerce in its entirety by whatever system it might de-

vise, but he carefully distinguished interstate commerce from that which was wholly within the states, and expressly conceded that the commerce which was wholly intrastate was wholly within the authority of the state.

The Employers Liability Cases, supra, expressly recognizes and enforces this distinction that, although Congress may set up a system of regulations affecting interstate commerce it must keep its hands entirely off intrastate trade.

In the case of Railway vs. Interstate Commerce Commission, 162 U. S. 184, the same limitation of the power of Congress is again recognized.

It might also be said that the Federal government has set up a system of controlling the sale of narcotics and could therefore follow the ramifications of the business throughout its whole area, but as we have already seen in the case of Linder vs. United States, supra, this court compelled the Federal government to stop as it was about to overstep its constitutional limits.

It therefore seems clear that Congress cannot by setting up one institution or a class of institutions for national purposes gather unto itself the power to control other institutions which are just as clearly creatures of the state government and exercising intrastate functions. The end does not justify the means when the means are expressly or impliedly forbidden.

7. Again it may be argued that the state bank by voluntarily accepting the provisions of the Federal Reserve act has placed itself within the authority and control of Congress.

This argument is fallacious in any case involving violations of constitutional restrictions, but it is particu-

larly unsound as applied to this statute. The statute does not aim merely to punish the state bank and its officers but attempts to penalize those who are legally strangers to the state bank. This case is an instance of it. The respondent, Westfall, a stranger to the Commercial Savings Bank, was indicted for aiding and abetting an officer of the bank and for conspiring with an officer of the bank. It can not possibly be maintained that persons wholly unassociated with the bank can be deprived of their constitutional guaranties by any acquiescence of the bank in the provisions of an unconstitutional statute.

But, as we have said, the contention that a citizen or corporation can be deprived of its constitutional guaranties by being induced to consent thereto is unsupportable in any case.

The constitution has divided the sovereign powers ordinarily exercised by governments for the benefit and protection of their citizens, and has placed a part of these powers exclusively within the control of Congress. How oppressive it would be, therefore, if the Federal government were permitted to say to its citizens: "We have in our custody certain beneficial powers which you may enjoy only on condition that you surrender to us other powers which you have heretofore expressly withheld."

The fallacious contention which we have mentioned was unanswerably refuted by Mr. Justice White in the Employers Liability Cases, supra, at page 502 in the following language:

> "It remains only to consider the contention which we have previously quoted, that the act is constitutional, although it embraces subjects not within the power of Congress to regulate commerce, because

one who engages in interstate commerce thereby submits all his business concerns to the regulating power of Congress. To state the proposition is to refute it. It assumes that because one engages in interstate commerce he thereby endows Congress with power not delegated to it by the Constitution, in other words, with the right to legislate concerning matters of purely state concern. It rests upon the conception that the constitution destroyed that freedom of commerce which it was its purpose to preserve, since it treats the right to engage in interstate commerce as a privilege which cannot be availed of except upon such conditions as Congress may prescribe, even although the conditions would be otherwise beyond the power of Congress. It is apparent that if the contention were well founded it would extend the power of Congress to every conceivable subject, however inherently local, would obliterate all the limitations of power imposed by the Constitution, and would destroy the authority of the states as to all conceivable matters which from the beginning have been, and must continue to be, under their control so long as the constitution endures."

To the same effect see Schowllenberger vs. Pennsylvania, 171 U. S. 1, and Collins vs. New Hampshire, 171 U. S. 30.

In these cases this court held that Congress had no power to forbid the transportation of legitimate and harmless products in interstate commerce for a lawful and proper purpose by requiring oleomargerine to be colored in such a manner as would render it unmarketable when sold in competition with other products intended for the same purpose.

We submit that the rule laid down by Mr. Justice White, above, applies with great force to the statute now under consideration. If Congress can exact from state banking institutions a surrender to Federal authority of this particular police power as a condition for the

conferring by Congress of great benefits which the citizens of the state have a natural right to enjoy, then there is no discernible limit at which we may expect the national government to stop. It may similarly acquire the right to govern the most ordinary of commercial transactions, the negotiation of paper, the acceptance of deposits, the form of secured loans and the manner of signing checks. It could demand from the state the right to control the hours of opening and closing the banks, the hours of labor therein and the issuing and sale of stock. State banks would cease to exist except in name, except in those rare instances of banks who did not desire to avail themselves of the great benefits naturally enjoyed under the Federal Reserve system. The price of refusal to surrender would be isolation and stagnation.

The same things may be said of practically every form of commercial and industrial organiaztion and activity. Congress undoubtedly has power to regulate the conduct of warehouses in their relations to interstate commerce. If it can interfere in the intrastate affairs of local warehouses as a condition to permitting such warehouses to receive the benefits of interstate commerce then the national government can gather unto itself absolute domination of the agricultural and commercial life of the people.

8. If we once concede that the national government has control of this field of legislation, even though that field be held concurrently with the states, we must also be ready to admit that Congress may exclude the states from control or regulation within this field. We believe that we are justified in assuming that if the statute under

consideration is upheld this court will eventually be compelled to rule that the Federal statute is supreme to the extent that it renders a state statute for the punishment of a similar crime invalid. In order that it may not appear that our fears are unfounded let us refer to the Michigan statute which has heretofore been available to the courts of Michigan for the punishment of the same crimes described in the Federal statute now before us. We refer to Sec. 8027 Compiled Laws of Michigan of 1915, being Sec. 58 of Act 205 of Public Acts of 1887. The section referred to reads as follows:

> "Section 58. Every president, director, cashier, treasurer, teller, clerk or agent of any bank, who embezzles, abstracts or willfully misapplies any of the moneys, funds, credits or property of the bank, whether owned by it or held in trust, or who, without authority of the directors, issues or puts forth any certificate of deposit, draws any order or bill of exchange, makes any acceptance, assigns any note, bond, draft, bill of exchange, mortgage, judgment or decree, or who makes any false entry in any book, report or statement of the bank, with intent in either case to injure or defraud the bank, or any company, corporation or person or to deceive any officer of the bank or any agent appointed to examine the affairs of such bank, and any person who with like intent aids or abets any officer, clerk, or agent, in violation of this section, or who shall issue or cause to be issued, or put in circulation, any bill, note or other evidence of debt to circulate as money, upon conviction thereof, shall be imprisoned in the state prison or in the state house of correction and reformatory at Ionia, not to exceed twenty years."

The State of Michigan has seen fit to punish an offense of this kind against its banks by imprisonment not to exceed twenty years as compared with a penalty imposed by the Federal statute of not more than five years.

Numerous convictions have been had under the Michigan statute, some of which have reached the court of last resort of the state. It needs no argument to show how greatly state power and authority will be impaired if Federal authority is permitted to possess this field of control.

In this discussion we have in mind the language found in Collins vs. New Hampshire, 171 U. S. 34.

> "The direct and necessary result of a statute must be taken into consideration when deciding as to its validity, even if that result is not in so many words either enacted or distinctly provided for. In whatsoever language a statute may be found, its purpose must be determined by its natural and reasonable effect."

This principle has been recognized by this court in other cases.

> Henderson vs. Mayor of New York, 92, U. S. 259.
> Morgan Steamship Company vs. Louisiana, 118 U. S. 462.

The state cannot divest itself of police power, because that is necessary to its very existence. One is a part of the other and neither can exist without the other. It seems to have been thought advisable by the framers of Sec. 5209 to take the powers usually exercised by the states and place them in Federal hands, perhaps distrusting the ability of the states to enforce their own laws. This method is as unsound in theory as it is in law. The dignity and authority of the state cannot be built up by weakening its necessary functions. The body of the state's power cannot be strengthened by denying it the privilege of exercise. To continue this course

would be to make sovereign states merely dependent tributaries. The present commanding position of the Union has been attained by the erection of a powerful federation composed of individually powerful states, each voluntarily yielding to the other supremacy in certain fields, and each jealously holding for itself the dominion over others. State governments and state institutions cannot under our present form of government be forced into the status of mere mouth-pieces of the will of Congress in state affairs.

We believe that we have established that there is no power to be implied from the constitution by which Congress can impose a penalty for an offense against a state bank as has been attempted in this instance. It will not be claimed that there is any express power giving the statute validity. We believe that the authority attempted to be exercised is wholly remote from the fields of control delegated to the national government. We insist that it is neither a necessary nor appropriate means of exercising any proper national function under the constitution.

We therefore submit that the answer of this court to the inquiry of the Circuit Court of Appeals *whether or not Section* 5209 *is constitutional as applied to state banks* should be "No".

Respectfully submitted,

JEWELL, FACE & MESSINGER,
Attorneys for Plaintiff in Error.

No. [illegible]

In the Supreme Court of the United States

October Term, [illegible]

C. O. W[illegible]

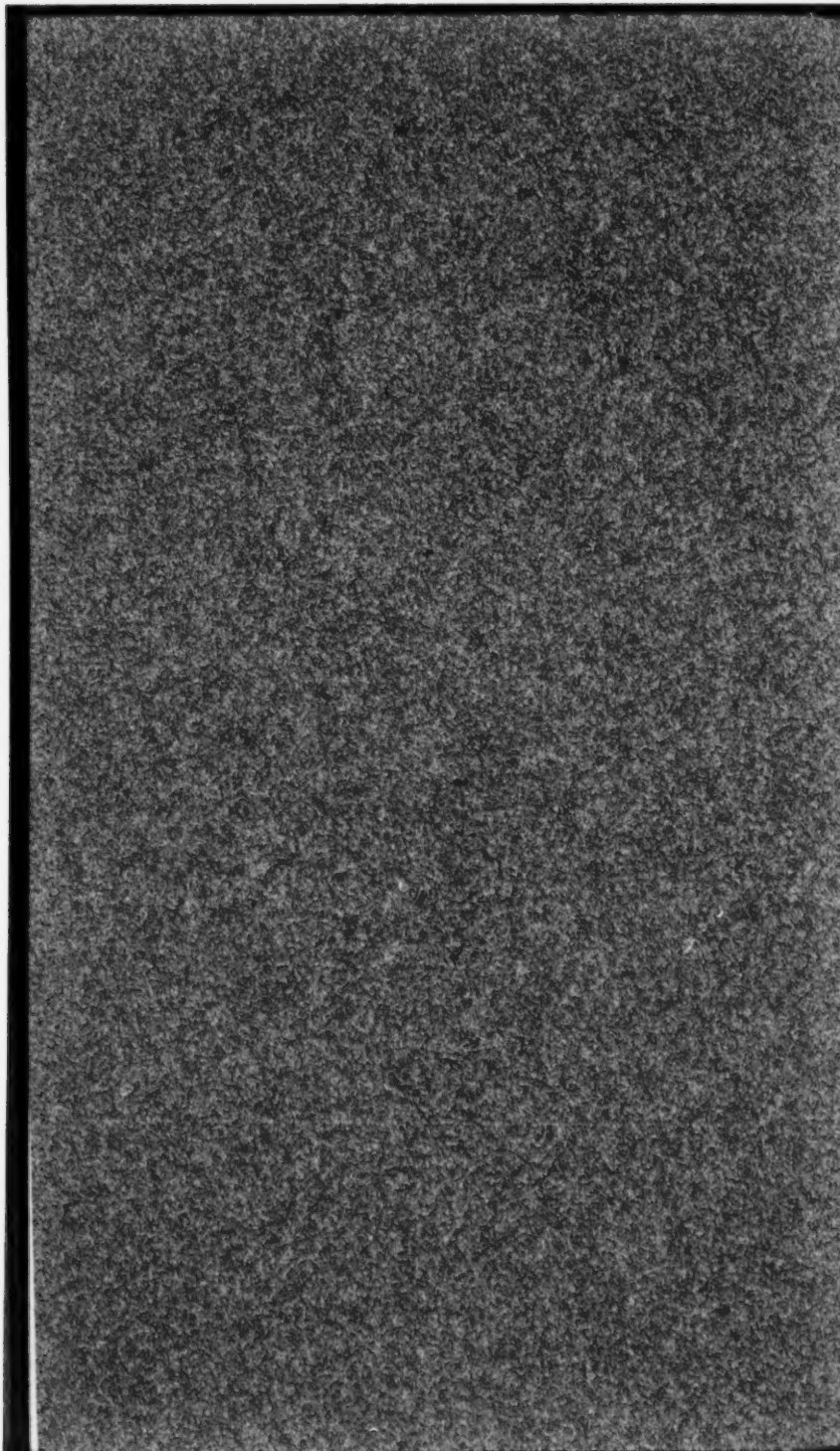
v.

The United States of America

ON CERTIFICATE FROM THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE UNITED STATES

[illegible]



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CITATIONS

In the Supreme Court of the United States

OCTOBER TERM, 1926

No. 766

C. O. WESTFALL

v.

THE UNITED STATES OF AMERICA

ON CERTIFICATE FROM THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE UNITED STATES

OPINION BELOW

As the case comes here on certificate from the Circuit Court of Appeals, no opinion was rendered below.

JURISDICTION

The jurisdiction of the Court to answer the question certified by the Circuit Court of Appeals is conferred by Section 239 of the Judicial Code, as amended by the Act of February 13, 1925.

THE QUESTION

The question certified is:

> Is the provision of Section 9, Chapter 6, of the Federal Reserve Act of December 23, 1913, as amended June 21, 1917, and July 1,

> 1922, constitutional in so far as it provides that "such banks and the officers, agents and employes thereof shall also be subject to the provisions of and to the penalties prescribed by Section 5209 of the Revised Statutes"?

The section of the Revised Statutes referred to makes it an offense for an officer or an employee of a Federal Reserve or member bank to embezzle or misapply its funds. The ultimate question in this case is whether State banks, members of the Federal Reserve system, are agencies of the United States, so that the United States has power to protect them by penal legislation from embezzlement of their funds.

THE STATUTES

That portion of the Federal Reserve Act of December 23, 1913 (c. 6, 38 Stat. 251, 260), set forth in Section 9 thereof, which makes the provisions of Section 5209, R. S., applicable to misconduct of officers, agents, and employees of member banks, reads as follows:

> Such banks, and the officers, agents, and employees thereof, shall also be subject to the provisions of and to the penalties prescribed by sections fifty-one hundred and ninety-eight, fifty-two hundred, fifty-two hundred and one, and fifty-two hundred and eight, and fifty-two hundred and nine of the Revised Statutes. * * *

Section 5209 of the Revised Statutes of the United States as amended by the Act of September 26, 1918

(c. 177, 40 Stat. 967, 972), so far as pertinent, reads as follows:

> Any officer, director, agent, or employee of any Federal reserve bank, or of any member bank as defined in the Act of December twenty-third, nineteen hundred and thirteen, known as the Federal reserve Act, who embezzles, abstracts, or willfully misapplies any of the moneys, funds, or credits of such Federal reserve bank or member bank, or who, without authority from the directors of such Federal reserve bank or member bank, issues or puts in circulation any of the notes of such Federal reserve bank, or member bank, or who, without such authority, issues or puts forth any certificate of deposit, draws any order or bill of exchange, makes any acceptance, assigns any note, bond, draft, bill of exchange, mortgage, judgment, or decree, or who makes any false entry in any book, report, or statement of such Federal reserve bank or member bank, with intent in any case to injure or defraud such Federal reserve bank or member bank, or any other company, body politic or corporate, or any individual person, or to deceive any officer of such Federal reserve bank or member bank, or the Comptroller of the Currency, or any agent or examiner appointed to examine the affairs of such Federal reserve bank or member bank, or the Federal Reserve Board; and every receiver of a national banking association who, with like intent to defraud or injure, embezzles, abstracts, purloins, or willfully misapplies any of the moneys,

Section 4 of the same Act reads in part as follows:

> Every Federal reserve bank shall be conducted under the supervision and control of a board of directors.
>
> The board of directors shall perform the duties usually appertaining to the office of directors of banking associations and all such duties as are prescribed by law.
>
> Said board shall administer the affairs of said bank fairly and impartially and without discrimination in favor of or against any member bank or banks and shall, subject to the provisions of law and the orders of the Federal Reserve Board, extend to each member bank such discounts, advancements and accommodations as may be safely and reasonably made with due regard for the claims and demands of other member banks.

Section 9 of the same Act as amended by the Act of June 21, 1917 (c. 32, 40 Stat. 232), and by the Act of March 4, 1923 (c. 252, 42 Stat. 1454, 1478), reads in part as follows:

> Any bank incorporated by special law of any State, or organized under the general laws of any State or of the United States, desiring to become a member of the Federal Reserve System, may make application to the Federal Reserve Board, under such rules and regulations as it may prescribe, for the right to subscribe to the stock of the Federal reserve bank organized within the district in which the applying bank is located. Such application shall be for the same amount of stock that the applying bank would be required to subscribe

to as a national bank. The Federal Reserve Board, subject to such conditions as it may prescribe, may permit the applying bank to become a stockholder of such Federal reserve bank.

In acting upon such applications the Federal Reserve Board shall consider the financial condition of the applying bank, the general character of its management, and whether or not the corporate powers exercised are consistent with the purposes of this Act.

Whenever the Federal Reserve Board shall permit the applying bank to become a stockholder in the Federal reserve bank of the district its stock subscription shall be payable on call of the Federal Reserve Board, and stock issued to it shall be held subject to the provisions of this Act.

All banks admitted to membership under authority of this section shall be required to comply with the reserve and capital requirements of this Act and to conform to those provisions of law imposed on national banks which prohibit such banks from lending on or purchasing their own stock, which relate to the withdrawal or impairment of their capital stock, and which relate to the payment of unearned dividends. * * *

As a condition of membership such banks shall likewise be subject to examinations made by direction of the Federal Reserve Board or of the Federal reserve bank by examiners selected or approved by the Federal Reserve Board.

* * * * *

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held for its account by the Federal reserve bank * * *.

Upon the indorsement of any of its member banks, which shall be deemed a waiver of demand, notice and protest by such bank as to its own indorsement exclusively, any Federal reserve bank may discount notes, drafts, and bills of exchange arising out of actual commercial transactions; that is, notes, drafts, and bills of exchange issued or drawn for agricultural, industrial, or commercial purposes, or the proceeds of which have been used, or are to be used, for such purposes, the Federal Reserve Board to have the right to determine or define the character of the paper thus eligible for discount, within the meaning of this Act. Nothing in this Act contained shall be construed to prohibit such notes, drafts, and bills of exchange, secured by staple agricultural products, or other goods, wares, or merchandise from being eligible for such discount, and the notes, drafts, and bills of exchange of factors issued as such making advances exclusively to producers of staple agricultural products in their raw state shall be eligible for such discount * * *.

Upon the indorsement of any of its member banks, which shall be deemed a waiver of demand, notice, and protest by such bank as to its own indorsement exclusively, and subject to regulations and limitations to be prescribed by the Federal Reserve Board, any Federal reserve bank may discount or purchase bills of exchange payable at sight or on demand

which are drawn to finance the domestic shipment of nonperishable, readily marketable staple agricultural products and are secured by bills of lading or other shipping documents conveying or securing title to such staples * * *.

* * * * *

Any member bank may accept drafts or bills of exchange drawn upon it having not more than six months sight to run, exclusive of days of grace, which grow out of transactions involving the importation or exportation of goods; or which grow out of transactions involving the domestic shipment of goods provided shipping documents conveying or securing title are attached at the time of acceptance; or which are secured at the time of acceptance by a warehouse receipt or other such document conveying or securing title covering readily marketable staples. No member bank shall accept, whether in a foreign or domestic transaction, for any one person, company, firm, or corporation to an amount equal at any time in the aggregate to more than ten per centum of its paid-up and unimpaired capital stock and surplus, unless the bank is secured either by attached documents or by some other actual security growing out of the same transaction as the acceptance; and no bank shall accept such bills to an amount equal at any time in the aggregate to more than one-half of its paid-up and unimpaired capital stock and surplus: *Provided, however*, That the Federal Reserve Board, under such general regulations as it may prescribe, which shall apply to all banks

alike regardless of the amount of capital stock and surplus, may authorize any member bank to accept such bills to an amount not exceeding at any time in the aggregate one hundred per centum of its paid-up and unimpaired capital stock and surplus * * *.

Any Federal reserve bank may make advances to its member banks on their promissory notes for a period not exceeding fifteen days at rates to be established by such Federal reserve banks, subject to the review and determination of the Federal Reserve Board, provided such promissory notes are secured by such notes, drafts, bills of exchange, or bankers' acceptances as are eligible for rediscount or for purchase by Federal reserve banks under the provisions of this Act, or by the deposit or pledge of bonds or notes of the United States.

* * * * *

Any member bank may accept drafts or bills of exchange drawn upon it having not more than three months' sight to run, exclusive of days of grace, drawn under regulations to be prescribed by the Federal Reserve Board, by banks or bankers in foreign countries or dependencies or insular possessions of the United States for the purpose of furnishing dollar exchange as required by the usages of trade in the respective countries, dependencies, or insular possessions. * * *

Section 13 (a) of the same Act, added by the Act of March 4, 1923 (c. 252, 42 Stat. 1454, 1479), provides in part as follows:

Upon the indorsement of any of its member banks, which shall be deemed a waiver of demand, notice, and protest by such bank as to its own indorsement exclusively, any Federal reserve bank may, subject to regulations and limitations to be prescribed by the Federal Reserve Board, discount notes, drafts, and bills of exchange issued or drawn for an agricultural purpose, or based upon live stock, and having a maturity, at the time of discount, exclusive of days of grace, not exceeding nine months, and such notes, drafts, and bills of exchange may be offered as collateral security for the issuance of Federal reserve notes under the provisions of section 16 of this Act * * *.

Section 15 of the same Act reads as follows:

The moneys held in the general fund of the Treasury, except the five per centum fund for the redemption of outstanding national-bank notes and the funds provided in this Act for the redemption of Federal reserve notes may, upon the direction of the Secretary of the Treasury, be deposited in Federal reserve banks, which banks, when required by the Secretary of the Treasury, shall act as fiscal agents of the United States; and the revenues of the Government or any part thereof may be deposited in such banks, and disbursements may be made by checks drawn against such deposits.

No public funds of the Philippine Islands, or of the postal savings, or any Government

> funds, shall be deposited in the continental United States in any bank not belonging to the system established by this Act: *Provided, however,* That nothing in this Act shall be construed to deny the right of the Secretary of the Treasury to use member banks as depositories. * * *

Section 16 of the same Act as amended by the Act of September 7, 1916 (c. 461, 39 Stat. 752, 754), and by the Act of June 21, 1917 (c. 32, 40 Stat. 232, 236, 238), provides in part as follows:

> Federal reserve notes, to be issued at the discretion of the Federal Reserve Board for the purpose of making advances to Federal reserve banks through the Federal reserve agents as hereinafter set forth and for no other purpose, are hereby authorized. The said notes shall be obligations of the United States and shall be receivable by all national and member banks and Federal reserve banks and for all taxes, customs, and other public dues. They shall be redeemed in gold on demand at the Treasury Department of the United States, in the city of Washington, District of Columbia, or in gold or lawful money at any Federal reserve bank.
>
> Any Federal reserve bank may make application to the local Federal reserve agent for such amount of the Federal reserve notes hereinbefore provided for as it may require. Such application shall be accompanied with a tender to the local Federal reserve agent of collateral in amount equal to the sum of the Federal reserve notes thus applied for and issued pursuant to such application. The collateral security thus offered shall be notes,

drafts, bills of exchange, or acceptances acquired under the provisions of section thirteen of this Act, or bills of exchange indorsed by a member bank of any Federal reserve district and purchased under the provisions of section fourteen of this Act, or bankers' acceptances purchased under the provisions of said section fourteen, or gold or gold certificates; but in no event shall such collateral security, whether gold, gold certificates, or eligible paper, be less than the amount of Federal reserve notes applied for. * * *

* * * * *

Every Federal reserve bank shall receive on deposit at par from member banks or from Federal reserve banks checks and drafts drawn upon any of its depositors, and when remitted by a Federal reserve bank, checks and drafts drawn by any depositor in any other Federal reserve bank or member bank upon funds to the credit of said depositor in said reserve bank or member bank. * * *

The Federal Reserve Board shall make and promulgate from time to time regulations governing the transfer of funds and charges therefor among Federal reserve banks and their branches, and may at its discretion exercise the functions of a clearing house for such Federal reserve banks, or may designate a Federal reserve bank to exercise such functions, and may also require each such bank to exercise the functions of a clearing house for its member banks. * * *

Section 19 of the same Act as amended by the Act of August 15, 1914 (c. 252, 38 Stat. 691), and by the

Act of June 21, 1917 (c. 32, 40 Stat. 232, 239), reads in part as follows:

> The required balance carried by a member bank with a Federal reserve bank may, under the regulations and subject to such penalties as may be prescribed by the Federal Reserve Board, be checked against and withdrawn by such member bank for the purpose of meeting existing liabilities: *Provided, however*, That no bank shall at any time make new loans or shall pay any dividends unless and until the total balance required by law is fully restored.

Section 5 of the Federal Farm Loan Act of July 17, 1916 (c. 245, 39 Stat. 360, 365), provides in part as follows:

> At least twenty-five per centum of that part of the capital of any Federal land bank for which stock is outstanding in the name of national farm loan associations shall be held in quick assets, and may consist of cash in the vaults of said land bank, or in deposits in member banks of the Federal reserve system, or in readily marketable securities which are approved under rules and regulations of the Federal Farm Loan Board: *Provided*, That not less than five per centum of such capital shall be invested in United States Government bonds.

Section 13 of the same Act reads in part as follows:

> That every Federal land bank shall have power, subject to the limitations and requirements of this Act—
>
> * * * * *

> Fifth. To deposit its securities, and its current funds subject to check, with any member bank of the Federal Reserve System, and to receive interest on the same as may be agreed.

Section 27 of the same Act reads in part as follows:

> Any member bank of the Federal Reserve System may buy and sell farm loan bonds issued under the authority of this Act.

By Section 15 of the War Finance Corporation Act of April 5, 1918 (c. 45, 40 Stat. 506, 510), and Section 212 of the Agricultural Credits Act of March 4, 1923 (c. 252, 42 Stat. 1454, 1469), member banks of the Federal Reserve System, were made authorized depositories for funds of the War Finance Corporation and the National Agricultural Credit Corporations.

SUMMARY OF ARGUMENT

The member banks of the Federal reserve system, whether corporations organized under State law or Act of Congress, are essential parts of that system. By reason of their relation to the system, they are instrumentalities of the Federal Government, and because of that the United States has a direct interest in protecting them in their capacity to function as a part of the Federal reserve system.

Congress has power to use State corporations as instrumentalities of the Federal Government.

ARGUMENT

THE MEMBER BANKS OF THE FEDERAL RESERVE SYSTEM, WHETHER CORPORATIONS ORGANIZED UNDER STATE LAW OR ACT OF CONGRESS, ARE INSTRUMENTALITIES OF THE FEDERAL GOVERNMENT, WHICH IT HAS THE POWER TO PROTECT

The provisions of the Federal Reserve Act disclose that the member banks of the Federal reserve system, national banks and State banks alike, play an important and essential part in carrying out the purposes of the statute. The member banks are the stockholders in and furnish the capital of the Federal reserve banks. It is through their membership in the Federal reserve system and through deposits in Federal reserve banks that the member banks maintain their reserves, and it is through the maintenance of such reserves by the member banks that the Federal reserve banks are enabled to control and use the banking reserves of the country to the best advantage.

It is upon the volume of commercial paper coming into the hands of member banks and endorsed by them and rediscounted by the Federal reserve banks that the volume of elastic currency very largely depends. The Federal reserve notes supplied by this system to expand and contract the currency of the country as conditions require are issued to the Federal reserve banks by the United States upon a pledging by the banks of collateral security, an important part of which is commercial paper acquired by the Federal reserve banks from the member banks and which

bears the endorsement of member banks. The provisions for a safe and elastic currency and the creation of a real and available reserve depend upon the member banks. Without them the Federal reserve system would not function. The financial stability of the member banks is of prime importance to the system. They are as much agencies or instrumentalities of the United States as are the Federal reserve banks. It is of no consequence that some of the member banks are corporations organized under State law and some of them are national banks organized under Acts of Congress. As member banks their relations to the Federal reserve system are substantially the same. In the execution of any power resting in the United States under the Constitution, Congress may employ as instrumentalities corporations organized under State law.

Cherokee Nation v. *Southern Kansas Ry. Co.*, 135 U. S. 641.

California v. *Pacific R. R. Co.*, 127 U. S. 1.

> Nothing in the Constitution forbids the selection of a state corporation as a national agent. In reason the material thing is the principal's authority, not the parentage or birthplace of the agent. (*Latinette* v. *City of St. Louis*, 201 Fed. 676, 679.)

It has long been established that Congress has power, by appropriate legislation, to protect agencies or instrumentalities of the United States against attack or injury which would interfere with the performance of their functions or impair their efficiency

as such. *United States* v. *Walter*, 263 U. S. 15. There, construing a statute which made the criminal laws respecting the defrauding of the United States apply to "any corporation in which the United States of America is a stockholder," the Court held it referred only to corporations, like the Fleet Corporation, which are instrumentalities of the Government and in which, for that reason, the United States owns stock. It said the fraud, if successful, "even more immediately would have impaired the efficiency of its very important instrument."

> See *In re Neagle*, 135 U. S. 1; *Thornton* v. *United States*, 271 U. S. 414; *In re Quarles and Butler*, 158 U. S. 532, 535; *McCulloch* v. *Maryland*, 4 Wheat. 316; *Osborn* v. *United States Bank*, 9 Wheat. 738; *Van Allen* v. *The Assessors*, 3 Wall. 573; *Logan* v. *United States*, 144 U. S. 263, 293.

An Act of Congress which makes it a penal offense to embezzle funds of a State bank, a member of the Federal Reserve system, does not infringe on any State power or prevent the State from punishing the offense. The same Act may constitute an offense against each of the two sovereignties. *United States* v. *Lanza*, 260 U. S. 377.

On the theory that member banks, whether State or Federal corporations, are agencies and instrumentalities of the United States, Congress has not only provided for punishment of those who misappropriate their funds, but has regulated State member banks by requiring them to comply with the reserve

and capital requirements of the Act, and to conform to those provisions of law imposed upon national banks, which prohibit such banks from lending on or purchasing their own stock, which relate to withdrawal or impairment of their capital stock, and which relate to the payment of unearned dividends.

All of these provisions must stand or fall together with the one here under consideration. It is evident that the discharge of their functions by the Federal reserve banks can be assured only as the activities and the continuance as going concerns of member banks are maintained. Member banks are by statute made essential factors in carrying out the purposes of the Act and have been selected as Federal instrumentalities under the wide latitude and discretion which is always accorded the Congress in determining whether any agency it selects is appropriate or necessary. If instead of utilizing State corporations as member banks Congress had itself created the member banks as it did the Federal reserve banks, doubtless it would be conceded that such banks would be Federal agencies. The mere fact that some of the agencies selected were corporations organized under State statutes does not make them any less agencies of the United States. They are as much agencies of the United States as are the Federal land banks. *Smith* v. *Kansas City Title Co.*, 255 U. S. 180. Anything that impairs or destroys the integrity of the member banks to that extent interferes with and hampers the operation of the Federal reserve system.

Westfall's contentions are plainly contrary to established principles.

In *Hiatt* v. *United States*, 4 F. (2d) 374, the Circuit Court of Appeals for the Seventh Circuit considered the question here presented and said (p. 377):

> When the Federal Reserve System was created, the banking business of the states and of the nation was done by national banks incorporated under federal law, state banks incorprated under state laws, and unincorporated private banks. While there had necessarily grown up business relations between the various banks, regardless of their origin, they were largely voluntary. Without going fully into the causes which produced the Federal Reserve System or the purposes of its creation, further than those expressed in the title, viz. "To provide for the establishment of Federal Reserve Banks, to furnish an elastic currency, to afford means of rediscounting commercial paper, to establish a more effective supervision of banking in the United States, and for other purposes," it is sufficient to say that it had long been recognized that for the purpose of carrying on undisturbed the necessary business and financial operations of the government some system should be devised whereby the banking operations of the country could be controlled and sudden and violent crises in financial affairs prevented. If, in the wisdom of Congress, it seemed that the inclusion of state banks and trust companies would contribute to such and other legitimate purposes of the Federal Reserve System, the

> right to so include them would seem not now open to question. The government may make use of concerns incorporated under state charters. *Latinette* v. *City of St. Louis*, 201 F. 676, 120 C. C. A. 638, decided by this court; *Cherokee Nation* v. *Kansas Ry. Co.*, 135 U. S. 641, 10 S. Ct. 965, 34 L. Ed. 295; *California* v. *Pacific R. R. Co.*, 127 U. S. 1, 8 S. Ct. 1073, 32 L. Ed. 150. The provision for membership of state banks in the Federal Reserve System is in no sense compulsory. We are of opinion that Congress was clearly within its constitutional rights in authorizing the admission of state banks and trust companies to the privileges and benefits of member banks in the Federal Reserve System.

In disposing of the immediate question, the court said (p. 377):

> It is urged that the provisions of section 5209 (Comp. St. § 9772), supra, as thus applied are repugnant to the federal Constitution and beyond the power of Congress, the theory being that they necessarily withdraw from the state the power to enact criminal laws with respect to the same offenses and suspend the operation of such criminal statutes touching the offenses enumerated in the section. The main reliance, in support of this contention, is upon *Easton* v. *Iowa*, 188 U. S. 221, 23 S. Ct. 288, 47 L. Ed. 452. That case and others cited are examples of attempts on the part of the state to punish, as criminal, certain acts done, not only by officers of state banks, but also by officers of national banks,

> and the Supreme Court held that such statutes, as applied to national banks are void, but the reasons there urged have nothing to do with the question here involved. It is to be noted that the acts which were made offenses under section 5209 are those committed by officers of a state bank pertaining to matters affecting the relations between the member bank and the Federal Reserve Bank. It must be apparent that the commission of acts made punishable by that section would necessarily affect the relations between the member bank and the Federal Reserve Bank, and also would affect injuriously the Federal Reserve Bank System. * * *

In that case a petition for certiorari was filed in this Court May 8, 1925, and denied June 1, 1925. *Hiatt, Petitioner*, v. *United States*, 268 U. S. 704.

One of the questions raised by the petition for certiorari in that case (page 5) was:

> Are the provisions of the Federal Reserve Act constitutional in so far as they purport to incorporate State loan, trust and safe deposit companies into the Federal Reserve System as member banks, and are the Federal penal acts constitutional in so far as applicable to such state corporation.

The Circuit Court of Appeals for the Sixth Circuit, which certified this case here, does not appear to have had the *Hiatt* case called to its attention, as it is not mentioned in either brief in the Circuit Court of Appeals, nor in the brief filed in this Court on

behalf of Westfall. This may explain the action of the court below in certifying the case.

That Westfall, although not himself an officer or employee of the member bank, may be punished under Section 5209 of the Revised Statutes for aiding or abetting or conspiring with an officer of the bank is shown in *Coffin* v. *United States*, 156 U. S. 432, 447.

CONCLUSION

The question certified should be answered in the affirmative.

Respectfully submitted.

WILLIAM D. MITCHELL,
Solicitor General.
O. R. LUHRING,
Assistant Attorney General.
HARRY S. RIDGELY,
Attorney.
WALTER WYATT,
General Counsel, Federal Reserve Board.

MARCH, 1927.

○

SUPREME COURT OF THE UNITED STATES.

No. 766.—October Term, 1926.

C. O. Westfall,
vs.
The United States of America.

On Certificate from the United States Circuit Court of Appeals for the Sixth Circuit.

[May 16, 1927.]

Mr. Justice Holmes delivered the opinion of the Court.

Westfall was convicted under two indictments, the first of which charged him with aiding and procuring the branch manager of a State bank which was a member of the Federal Reserve System to misapply the funds of the bank. The second indictment charged a conspiracy to misapply the funds of the bank between the same and other parties. Both were based upon the issuing a fraudulent certificate of deposit for ten thousand dollars and the paying the same from the funds of the bank. The Circuit Court of Appeals for the Sixth Circuit certifies this question: "Is the provision of section 9, chapter 6, of the Federal Reserve Act of December 23, 1913 [38 Stat. 259, 260,] as amended June 21, 1917 [c. 32, § 3; 40 Stat. 232.] and July 1, 1922 constitutional in so far as it provides that 'such banks and the officers, agents and employees thereof shall also be subject to the provisions of and the penalties prescribed by Section 5209 of the Revised Statutes?'" The amendment of July 1, 1922, referred to is, we presume, c. 274; 42 Stat. 821. It has no immediate bearing upon the question propounded and as it is not relied upon in argument we shall leave it on one side.

It is not disputed that Rev. Stat. § 5209, if applicable, punishes the bank manager, and those who aided and abetted him in his crime. *Coffin* v. *United States*, 156 U. S. 432, 447. The argument is that Congress has no power to punish offences against the property rights of State banks. It is said that the statute is so broad that it covers such offences when they could not result in any loss to the Federal Reserve Banks, and it is suggested that if upheld the Act will invalidate similar statutes of the States. This argu-

ment is well answered by *Hiatt* v. *United States*, 4 F. (2d) 374, 377. Certiorari denied. 268 U. S. 704. Of course an act may be criminal under the laws of both jurisdictions. *United States* v. *Lanza*, 260 U. S. 377, 382. And if a state bank chooses to come into the System created by the United States, the United States may punish acts injurious to the System, although done to a corporation that the State also is entitled to protect. The general proposition is too plain to need more than statement. That there is such a System and that the Reserve Banks are interested in the solvency and financial condition of the members also is too obvious to require a repetition of the careful analysis presented by the Solicitor General. The only suggestion that may deserve a word is that the statute applies indifferently whether there is a loss to the Reserve Banks or not. But every fraud like the one before us weakens the member bank and therefore weakens the System. Moreover, when it is necessary in order to prevent an evil to make the law embrace more than the precise thing to be prevented it may do so. It may punish the forgery and utterance of spurious interstate bills of lading in order to protect the genuine commerce. *United States* v. *Ferger*, 250 U. S. 199. See further *Southern Ry. Co.* v. *United States*, 222 U. S. 20, 26. That principle is settled. Finally Congress may employ state corporations with their consent as instrumentalities of the United States, *Clallam County* v. *United States*, 263 U. S. 341, and may make frauds that impair their efficiency crimes. *United States* v. *Walter*, 263 U. S. 15. We answer the question:

Yes.

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